

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:B05

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### Legend

Distributing =

Controlled =

Shareholder 1 =

Shareholder 2 =

Business A =

Business B =

Distributing Property =

Shareholder Property =

Retained Distributing  
Property =

a =

b =

Dear \_\_\_\_\_ :

This letter responds to your March 29, 2013 request for rulings on certain federal income tax consequences of a series of proposed transactions. The information submitted in that letter and in subsequent correspondence is summarized below.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, this office has not reviewed any information pertaining to and has made no determination regarding whether the distribution described below (i) satisfies the business purpose requirement of Treas. Reg. § 1.355-2(b); (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation (see section 355(a)(1)(B) of the Internal Revenue Code of 1986, as amended, (the "Code") and Treas. Reg. § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest in the distributing corporation or the controlled corporation (see section 355(e)(2)(A)(ii) and Treas. Reg. § 1.355-7).

### **Facts**

Distributing has outstanding a single class of stock. Shareholder A and Shareholder B own all shares of Distributing stock, each owning a shares.

Distributing is engaged in both Business A and Business B. Distributing has submitted financial information indicating that Business A and Business B have had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Distributing holds Distributing Property that it uses for Business A and Business B. Additionally, Shareholder A and Shareholder B each hold a b percent undivided interest in Shareholder Property that Distributing uses for Business A and Business B.

### **Proposed Transaction**

For what have been represented to be valid business purposes, Distributing plans to complete the following steps pursuant to an overall plan (the "Proposed Transaction"):

- (i) Shareholder 2 will exchange his b percent undivided interest in Shareholder Property with Distributing in exchange for an amount of Distributing Property of equal value (the "Property Exchange").
- (ii) Distributing will form new corporation Controlled. Distributing will contribute Distributing Property it still holds after the Property Exchange, with the exception of Retained Distributing Property, and Business B assets to Controlled in exchange for all of the stock of Controlled (the "Contribution").
- (iii) Distributing will distribute to Shareholder 2 all of the stock of Controlled in exchange for all of Shareholder 2's stock in Distributing (the "Distribution").

Following the Contribution, Distributing will conduct Business A and Controlled will conduct Business B. Shareholder 1 and Distributing will each hold a b percent undivided interest in the Shareholder Property. Shareholder 2 will hold property he acquired in the Property Exchange.

Following the Distribution, it is anticipated that Distributing and Controlled may have agreements between them regarding the use of each other's business assets. Such use, and any transactions between Distributing and Controlled after the Distribution, will be pursuant to agreements negotiated at arm's length.

### **Representations**

- (a) Controlled will not be indebted to Distributing after the Distribution.
- (b) The fair market value of the Controlled stock to be received by Shareholder 2 will be approximately equal to the fair market value of the Distributing stock surrendered by Shareholder 2 in the exchange.
- (c) No part of the consideration to be distributed by Distributing will be received by Shareholder 2 as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.
- (d) The five years of financial information for Business A submitted on behalf of Distributing is representative of the present operation of Business A, and there have been no substantial operational changes since the date of the last financial statement submitted.
- (e) The five years of financial information for Business B before the Contribution submitted on behalf of Distributing is representative of the present operation of Business B, and there have been no substantial operational changes since the date of the last financial statement submitted.

- (f) Following the Proposed Transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (g) The Distribution is carried out for the following corporate business purposes: (i) enabling Shareholder 1 to focus all of his attention on managing Business A; (ii) allowing Controlled flexibility to pursue its strategic interest independent of Distributing; (iii) to maximize the economic performance of Distributing and Controlled; and (iv) to provide for the effective transition in management of Distributing or Controlled upon the retirement of Shareholder 1 and Shareholder 2. The Distribution is motivated in whole or in substantial part, by one or more of these corporate business purposes.
- (h) The Proposed Transaction is not being used primarily as a device for the distribution of earnings and profits of Distributing or Controlled or both.
- (i) The total adjusted basis of the assets transferred to Controlled by Distributing will equal or exceed the sum of the total amount of liabilities assumed (as determined under section 357(d) of the Code) by Controlled. The liabilities assumed in the transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- (j) The total fair market value of the assets transferred to Controlled by Distributing will exceed the sum of (i) the amount of liabilities assumed (as determined under Section 357(d) of the Code) by Controlled in connection with the transfer of assets and (ii) the amount of liabilities owed to Controlled by Distributing that are discharged or extinguished in connection with the transfer of assets.
- (k) The fair market value of the assets of Controlled will equal or exceed the amount of its liabilities immediately after the Distribution.
- (l) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (m) No inter-corporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution, except that Distributing may contribute to Controlled Distributing's note if it is necessary to equalize value between the stock of Distributing and of Controlled. Such note will have a term of no greater than five years and bear an interest rate based on market terms.
- (n) Payments made in connection with all continuing transactions between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

- (o) No parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv) of the Code.
- (p) There is no acquisition of stock of Distributing or Controlled (including any predecessor or successor of any such corporation) that is part of a plan or series of related transactions (within the meaning of Treas. Reg. § 1.355-7) that includes the distribution of Controlled stock.
- (q) Immediately after the transaction (as defined in section 355(g)(4)), either (i) no person will hold a 50-percent or greater interest (within the meaning of section 355(g)(3)) in Distributing or Controlled, (ii) if any person holds a 50 percent or greater interest (within the meaning of section 355(g)(3)) in any disqualified investment corporation (within the meaning of section 355(g)(2)), such person will have held such interest in such corporation immediately before the transaction, or (iii) neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of section 355(g)(2)).
- (r) For purposes of section 355(d), immediately after the Distribution, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the 5-year period (determined after applying section 355(d)(6)) ending on the date of the Distribution.
- (s) For purposes of section 355(d), immediately after the Distribution, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in section 355(d)(5) and (8)) during the 5-year period (determined after applying section 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five-year period (determined after applying section 355(d)(6)) ending on the date of the Distribution.

### **Rulings**

Based solely on the information submitted and the representations set forth above, we rule as follows:

- (1) The Contribution followed by the Distribution will constitute a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled each will be “a party to a reorganization” within the meaning of section 368(b).

- (2) No gain or loss will be recognized by Distributing on the Contribution (sections 361(a) and 357(a)).
- (3) No gain or loss will be recognized by Controlled on the Contribution (section 1032(a)).
- (4) Controlled's basis in each asset received from Distributing in the Contribution will equal the basis of such asset in the hands of Distributing immediately before the transfer (section 362(b)).
- (5) Controlled's holding period in each asset received from Distributing in the Contribution will include the holding period during which Distributing held such asset (section 1223(2)).
- (6) No gain or loss will be recognized by Distributing on the Distribution (section 361(c)).
- (7) Shareholder 2 will not recognize gain or loss (and will include no amount in income) upon his receipt of Controlled stock from Distributing (section 355(a)(1)).
- (8) The basis of Controlled stock in the hands of Shareholder 2 will equal the basis of Distributing stock surrendered in exchange thereof (section 358(a)(1)).
- (9) The holding period of the Controlled stock to be received by Shareholder 2 will include the holding period during which Shareholder 2 held the Distributing stock exchanged therefore, provided that the Distributing stock is held as a capital asset on the date of the exchange (section 1223(1)).
- (10) Earnings and profits will be allocated between Distributing and Controlled in accordance with section 312(h) and Treas. Reg. § 1.312-10(a).

### **Caveats**

Except as expressly provided herein, no opinion is expressed about the tax treatment of the Proposed Transaction or any other transaction or item mentioned in this letter under other provisions of the code or regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from, the foregoing that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding (i) whether the Property Exchange qualifies as an exchange under section 1031, (ii) whether the Distribution satisfies the business purpose requirement of Treas. Reg. § 1.355-2(b); (iii) whether the Distribution is used principally as a device for the distribution of the earnings and profits of Distributing, Controlled, or both; or (iv) whether

the Distribution is part of a plan (or a series of related transactions) under section 355(e)(2)(A)(ii).

### **Procedural Statements**

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

*Isaac W. Zimbalist*

Isaac W. Zimbalist  
Senior Technical Reviewer  
Office of Associate Chief Counsel (Corporate)